JSC PASHA Bank Georgia

Financial statements

Year ended 31 December 2018
together with independent auditor's report

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Independent auditor's report

To the Shareholders and Board of Directors of JSC PASHA Bank Georgia

Opinion

We have audited the financial statements of JSC PASHA Bank Georgia (the "Bank"), which comprise the statement of financial position as at 31 December 2018, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2018 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other information included in the Bank's 2018 Annual Report

Other information consists of the information included in Bank's 2018 Annual Report, other than the financial statements and our auditor's report thereon. Management is responsible for the other information. The Bank's 2018 Annual Report is expected to be made available to us after the date of this auditor's report.

Our opinion on the financial statements does not cover the other information and we will not express any form of assurance conclusion thereon in our report on the audit of the financial statements.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

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Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRSs, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Ruslan Khoroshvili

On behalf of EY LLC

Tbilisi, Georgia

14 March 2019

STATEMENT OF FINANCIAL POSITION

As at 31 December 2018

(Amounts in tables are in thousands of Georgian lari)

	Notes	2018	2017
Assets			
Cash and cash equivalents	5	46,503	43,908
Amounts due from credit institutions	6	63,105	51,445
Loans to customers	7	188,834	111,679
Investment securities	8	20,226	62,033
Property and equipment	9	2,136	906
Intangible assets	10	2,513	2,122
Deferred income tax assets	14	148	–
Other assets	11	3,592	711
Total assets		**327,057**	**272,804**
Liabilities			
Amounts due to credit institutions	12	110,262	106,402
Amounts due to customers	13	104,539	58,181
Provisions		74	135
Other liabilities	11	1,940	1,279
Total liabilities		**216,815**	**165,997**
Equity			
Share capital	15	103,000	103,000
Retained earnings		7,242	3,807
Total equity		**110,242**	**106,807**
Total equity and liabilities		**327,057**	**272,804**

Signed on behalf of the Board of Directors of the Bank on 14 March 2019:

Arda Yusuf Arkun — Chairman of the Board of Directors

Chingiz Abdullayev — Chief Financial Officer, Member of the Board of Directors

The accompanying selected explanatory notes on pages 8 to 53 are an integral part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2018

(Amounts in tables are in thousands of Georgian lari)

	Notes	2018	2017
Interest revenue calculated using effective interest rate			
Loans to customers		14,162	11,765
Investment securities		4,010	5,292
Amounts due from credit institutions		2,881	2,385
		21,053	**19,442**
Interest expense			
Amounts due to credit institutions		(3,868)	(3,099)
Amounts due to customers		(1,053)	(869)
		(4,921)	**(3,968)**
Net interest income		**16,132**	**15,474**
Credit loss expense on interest bearing assets		(1,517)	(1,041)
Net interest income after impairment losses		**14,615**	**14,433**
Net gains from foreign currencies			
dealing		2,484	1,190
translation differences		197	402
Net fee and commission income	17	390	255
Other operating income		28	230
Non-interest income		**3,099**	**2,077**
Personnel expenses	18	(8,258)	(5,420)
General and administrative expenses	18	(5,466)	(5,302)
Depreciation and amortisation	9,10	(952)	(1,351)
Provision for impairment losses		7	(32)
Other operating expenses		(4)	(28)
Non-interest expenses		**(14,673)**	**(12,133)**
Profit before income tax		**3,041**	**4,377**
Income tax benefit/(expense)	14	148	(924)
Net profit for the period		**3,189**	**3,453**
Other comprehensive income			
Other comprehensive income to be reclassified to profit or loss in subsequent periods			
Net unrealized gain on investments securities available for sale		–	70
Total comprehensive income for the year		**3,189**	**3,523**

The accompanying selected explanatory notes on pages 8 to 53 are an integral part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2018

(Amounts in tables are in thousands of Georgian lari)

	Share capital	Retained earnings	Other reserves	Total equity
1 January 2017	**103,000**	**354**	**(70)**	**103,284**
Profit for the year	–	3,453	–	3,453
Other comprehensive income for the year	–	–	70	70
Total comprehensive income for the year	**–**	**3,453**	**70**	**3,523**
31 December 2017	**103,000**	**3,807**	–	**106,807**
Impact of adopting IFRS 9 (Note 3)	**–**	246	**–**	**246**
Restated opening balance under IFRS 9	**103,000**	**4,053**	**–**	**107,053**
Profit for the year	–	3,189	–	3,189
Total comprehensive income for the year	**–**	**3,189**	**–**	**3,189**
31 December 2018	**103,000**	**7,242**	–	**110,242**

The accompanying selected explanatory notes on pages 8 to 53 are an integral part of these financial statements.

STATEMENT OF CASH FLOWS

For the year ended 31 December 2018

(Amounts in tables are in thousands of Georgian lari)

	Notes	2018	2017
Cash flows from operating activities			
Interest received		21,453	19,832
Interest paid		(5,158)	(3,919)
Fees and commissions received		774	214
Fees and commissions paid		(417)	(411)
Realised gains less losses from dealing in foreign currencies		2,484	1,190
Personnel expenses paid		(7,845)	(5,459)
General and administrative expenses paid		(6,899)	(5,557)
Other income received		28	230
Cash flows from operating activities before changes in operating assets and liabilities		**4,420**	**6,120**
Net (increase)/decrease in operating assets			
Amounts due from credit institutions		(6,441)	30,971
Loans to customers		(73,134)	(16,021)
Net increase/(decrease) in operating liabilities			
Amounts due to credit institutions		(1,999)	(24,414)
Amounts due to customers		42,251	12,539
Net cash (used in)/from operating activities		**(34,903)**	**9,195**
Cash flows from investing activities			
Purchase of investment securities		(6,226)	(47,941)
Proceeds from redemption of investment securities		47,763	77,027
Purchase of property and equipment		(2,250)	(803)
Proceeds from sale of property and equipment		28	61
Purchase of intangible assets		(1,470)	(339)
Net cash from investing activities		**37,845**	**28,005**
Effect of exchange rates changes on cash and cash equivalents		(347)	(891)
Net increase in cash and cash equivalents		**2,595**	**36,309**
Cash and cash equivalents, beginning	5	**43,908**	**7,599**
Cash and cash equivalents, ending	5	**46,503**	**43,908**

The accompanying selected explanatory notes on pages 8 to 53 are an integral part of these financial statements.

(Amounts in tables are in thousands of Georgian lari)

1. Principal activities

JSC PASHA Bank Georgia (the "Bank") was formed on 17 December 2012 as a joint stock company under the laws of Georgia. The Bank operates under a general banking license issued by the National Bank of Georgia (the "NBG") on 17 January 2013 (Identification code: 404433671).

The Bank accepts deposits and extends credit, transfers payments in Georgia and abroad, exchanges currencies and provides other banking services to its commercial customers. The shareholders of the Bank have approved a new strategy of the Bank for the next three year strategic period, based on which, several initiatives will be implemented by the Bank's management during 2019 and in the subsequent years to enter into retail markets.

Starting from 2017 the Bank is a member of the deposit insurance system. The system operates under the Law of Georgia on Deposit Insurance System and insures all types of deposits of resident and non-resident individuals up to GEL 5,000, with certain exceptions.

The Bank has one service office in Georgia as of 31 December 2018. The Bank's registered legal address is 15 Rustaveli Avenue, Tbilisi, 0108, Georgia.

As at 31 December 2018 and 2017, the Bank's 100% owner was OJSC PASHA Bank (the "Parent"), the Republic of Azerbaijan. The Bank is ultimately owned by Mrs. Leyla Aliyeva and Mrs. Arzu Aliyeva, who exercise joint control over the Bank.

These financial statements have not yet been approved by the Parent on the general meeting of shareholders of the Bank. The shareholders have the power and authority to amend the financial statements after the issuance.

2. Basis of preparation

General

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

The financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below.

These financial statements are presented in Georgian lari ("GEL"), unless otherwise indicated.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies

Changes in accounting policies

The Bank applied IFRS 15 "*Revenue from contracts with customers"* and IFRS 9 "*Financial instruments"* for the first time. The nature and effect of the changes as a result of adoption of these new accounting standards are described below.

The Bank has not early adopted any standards, interpretations or amendments that have been issued but are not yet effective. The nature and the impact of each amendment is described below.

IFRS 9 Financial Instruments

IFRS 9 replaces IAS 39 *Financial Instruments: Recognition and Measurement* for annual periods on or after 1 January 2018. The Bank has not restated comparative information for 2017 for financial instruments in the scope of IFRS 9. Therefore, the comparative information for 2017 is reported under IAS 39 and is not comparable to the information presented for 2018. Differences arising from the adoption of IFRS 9 have been recognised directly in retained earnings as of 1 January 2018 and are disclosed below.

(a) Classification and measurement

Under IFRS 9, all debt financial assets that do not meet a "solely payment of principal and interest" (SPPI) criterion, are classified at initial recognition as fair value through profit or loss (FVPL). Under this criterion, debt instruments that do not correspond to a "basic lending arrangement", such as instruments containing embedded conversion options or "non-recourse" loans, are measured at FVPL. For debt financial assets that meet the SPPI criterion, classification at initial recognition is determined based on the business model, under which these instruments are managed:

- Instruments that are managed on a "hold to collect" basis are measured at amortised cost;
- Instruments that are managed on a "hold to collect and for sale" basis are measured at fair value through other comprehensive income (FVOCI);
- Instruments that are managed on other basis, including trading financial assets, will be measured at FVPL

Equity financial assets are required to be classified at initial recognition as FVPL unless an irrevocable designation is made to classify the instrument as FVOCI. For equity investments classified as FVOCI, all realised and unrealised gains and losses, except for dividend income, are recognised in other comprehensive income with no subsequent reclassification to profit and loss.

The classification and measurement of financial liabilities remains largely unchanged from the current IAS 39 requirements. Derivatives will continue to be measured at FVPL. Embedded derivatives are no longer separated from a host financial asset.

(b) Impairment

The adoption of IFRS 9 has fundamentally changed the Bank's accounting for loan impairment by replacing IAS 39 incurred loss approach with a forward-looking expected credit loss (ECL) approach. From 1 January 2018, the Bank has been recording the allowance for expected credit losses for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts, in this section all referred to as 'financial instruments'. Equity instruments are not subject to impairment under IFRS 9.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

(b) Impairment (continued)

The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination. If the financial asset meets the definition of purchased or originated credit impaired (POCI), the allowance is based on the change in the ECLs over the life of the asset. Details of the Bank's impairment method are disclosed in Note 19. The quantitative impact of applying IFRS 9 as at 1 January 2018 is disclosed in section (c) below.

(c) Effect of transition to IFRS 9

The following tables set out the impact of adopting IFRS 9 on the statement of financial position and retained earnings as at 1 January 2018 including the effect of replacing IAS 39 incurred credit loss calculations with IFRS 9 ECL.

A reconciliation between the carrying amounts under IAS 39 to the balances reported under IFRS 9 as at 1 January 2018 is as follows:

	IAS 39 measurement			Remeasurement	IFRS 9	
	Ref	**Category**	**Amount**	**ECL**	**Amount**	**Category**
Assets						
Cash and cash equivalents	A	L&R[1]	43,908	–	43,908	Amortised cost
Amounts due from credit institutions	A	L&R	51,445	(49)	51,396	Amortised cost
Loans to customers	A	L&R	111,679	796	112,475	Amortised cost
Investment securities	A	L&R	62,033	(619)	61,414	Amortised cost
Other financial assets – derivative financial assets		FVPL[2]	62	–	62	FVPL
All other assets		–	3,677	–	3,677	–
Total assets			**272,804**	**128**	**272,932**	
Liabilities						
Provisions for guarantees and letters of credit			(135)	122	(13)	–
Provision for unused credit lines			–	(4)	(4)	
All other liabilities			(165,862)	–	(165,862)	–
Total liabilities			**(165,997)**	**118**	**(165,879)**	

1 L&R: Loans and receivables.
2 FVPL: Fair value through profit and loss

A. As of 1 January 2018, the Bank's analysis highlighted that all financial assets except for derivative financial assets meet the SPPI criterion. Therefore, this financial assets measured at amortised cost previously, under IAS 39, are classified by Bank as financial assets at amortized cost under IFRS 9.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

IFRS 9 Financial Instruments (continued)

The impact of transition to IFRS 9 on reserves and retained earnings is as follows:

	Retained earnings
Closing balance under IAS 39 (31 December 2017)	**3,807**
Recognition of IFRS 9 ECLs	246
Restated opening balance under IFRS 9 (1 January 2018)	**4,053**
Total change in equity due to adopting IFRS 9	**246**

The following table reconciles the aggregate opening loan loss allowances under IAS 39 and provisions for loan commitments and financial guarantee contracts in accordance with IAS 37 *Provisions Contingent Liabilities and Contingent Assets* to the ECL allowances under IFRS 9.

	Loan loss allowance/ provision under IAS 39 / IAS 37 at 31 December 2017	Remeasurement	ECL under IFRS 9 at 1 January 2018
Impairment allowance for:			
Loans and receivables at amortised cost	(3,098)	796	(2,302)
Amounts due from credit institutions	–	(49)	(49)
Investment securities at amortised cost	(246)	(619)	(865)
	(3,344)	**128**	**(3,216)**
Guarantees	(110)	98	(12)
Letters of credit	(25)	24	(1)
Unused credit lines	–	(4)	(4)
	(135)	**118**	**(17)**
	(3,479)	**246**	**(3,233)**

IFRS 15 Revenue from Contracts with Customers

IFRS 15, issued in May 2014, and amended in April 2016, establishes a five-step model to account for revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. However, the standard does not apply to revenue associated with financial instruments and leases, and therefore, does not impact the majority of the Bank's revenue including interest income, gains/(losses) on operations with securities which are covered by IFRS 9 *Financial Instruments*. As a result, the majority of the Bank's income is not impacted by the adoption of this standard.

IFRIC Interpretation 22 Foreign Currency Transactions and Advance Considerations

The Interpretation clarifies that, in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine the date of the transactions for each payment or receipt of advance consideration. This Interpretation does not have any impact on the Bank's financial statements.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Fair value measurement

Fair values of financial instruments measured at amortised cost are disclosed in Note 20.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- in the principal market for the asset or liability; or
- in the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible by the Bank. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. Fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 − quoted (unadjusted) market prices in active markets for identical assets or liabilities;
- Level 2 − valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable;
- Level 3 − valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Bank determines whether transfers have occurred between levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Financial assets and liabilities

Initial recognition

Date of recognition

All regular way purchases and sales of financial assets and liabilities are recognised on the trade date i.e. the date that the Bank commits to purchase the asset or liability. Regular way purchases or sales are purchases or sales of financial assets and liabilities that require delivery of assets and liabilities within the period generally established by regulation or convention in the marketplace.

Initial measurement

The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments. Financial instruments are initially measured at their fair value and, except in the case of financial assets and financial liabilities recorded at FVPL, transaction costs are added to, or subtracted from, this amount.

Measurement categories of financial assets and liabilities

From 1 January 2018, the Bank classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

- amortised cost;
- FVOCI;
- FVPL.

The Bank classifies and measures its derivative portfolio at FVPL. The Bank may designate financial instruments at FVPL, if so doing eliminates or significantly reduces measurement or recognition inconsistencies.

Before 1 January 2018, the Bank classified its financial assets as loans and receivables (amortised cost), FVPL or available-for-sale.

Financial liabilities, other than loan commitments and financial guarantees, are measured at amortised cost or at FVPL when they are held for trading, are derivative instruments or the fair value designation is applied.

Amounts due from credit institutions, loans to customers, investments securities at amortised cost

Before 1 January 2018, amounts due from credit institutions, loans to customers and investment securitites included non-derivative financial assets with fixed or determinable payments that were not quoted in an active market, other than those:

- that the Bank intended to sell immediately or in the near term;
- that the Bank, upon initial recognition, designated as at FVPL or as available-for-sale;
- for which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration, which were designated as available-for-sale.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Financial assets and liabilities (continued)

From 1 January 2018, the Bank only measures amounts due from credit institutions, loans to customers and investment securities at amortised cost if both of the following conditions are met:

- the financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows;
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI).

The details of these conditions are outlined below.

Business model assessment

The Bank determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective.

The Bank's business model is not assessed on an instrument-by-instrument basis, but at a higher level of aggregated portfolios and is based on observable factors such as:

- how the performance of the business model and the financial assets held within that business model are evaluated and reported to the entity's key management personnel;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way those risks are managed;
- how managers of the business are compensated (for example, whether the compensation is based on the fair value of the assets managed or on the contractual cash flows collected);
- the expected frequency, value and timing of sales are also important aspects of the Bank's assessment.

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Bank's original expectations, the Bank does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

The SPPI test

As a second step of its classification process the Bank assesses the contractual terms of financial asset to identify whether they meet the SPPI test.

'Principal' for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset (for example, if there are repayments of principal or amortisation of the premium/discount).

The most significant elements of interest within a lending arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Bank applies judgement and considers relevant factors such as the currency in which the financial asset is denominated, and the period for which the interest rate is set.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Financial assets and liabilities (continued)

In contrast, contractual terms that introduce a more than de minimis exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely payments of principal and interest on the amount outstanding. In such cases, the financial asset is required to be measured at FVPL.

Letters of credit and undrawn loan commitments

The Bank issues letters of credit and loan commitments. Undrawn loan commitments and letters of credits are commitments under which, over the duration of the commitment, the Bank is required to provide a loan with pre-specified terms to the customer. Under IAS 39, a provision was made if they were an onerous contract but, from 1 January 2018, these contracts are in the scope of the ECL requirements.

Performance guarantees

Performance guarantees are contracts that provide compensation if another party fails to perform a contractual obligation. Performance guarantees do not transfer credit risk. The risk under performance guarantee contracts is the possibility that the failure to perform the contractual obligation by another party occurs. Therefore, performance guarantees are not considered financial instruments and thus do not fall in scope of IFRS 9.

Loans and receivables

Before 1 January 2018, loans and receivables were non-derivative financial assets with fixed or determinable payments that were not quoted in an active market. They were not entered into with the intention of immediate or short-term resale. Such assets were carried at amortised cost using the effective interest method. Gains and losses were recognised in profit or loss when the loans and receivables were derecognised or impaired, as well as through the amortisation process.

Reclassification of financial assets and liabilities

Following adoption of IFRS 9, the Bank updated presentation of the statement of profit or loss to present impairment losses determined in accordance with IFRS 9 as a single line item. Accordingly, the following reclassifications of impairment charges on letters of credit and undrawn loan commitments have been made to 2017 statement of profit or loss to conform to the 2018 presentation.

	As previously reported	Reclassification	As adjusted
Credit loss expense on interest bearing assets	(1,023)	(18)	(1,041)
Provision for impairment losses	(50)	18	(32)

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Renegotiated loans

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions.

From 1 January 2018, the Bank derecognises a financial asset, such as a loan to a customer, when the terms and conditions have been renegotiated to the extent that, substantially, it becomes a new loan, with the difference recognised as a derecognition gain or loss, to the extent that an impairment loss has not already been recorded. The newly recognised loans are classified as Stage 1 for ECL measurement purposes, unless the new loan is deemed to be POCI. When assessing whether or not to derecognise a loan to a customer, amongst others, the Bank considers the following factors:

- change in currency of the loan;
- change in counterparty;
- if the modification is such that the instrument would no longer meet the SPPI criterion.

If the modification does not result in cash flows that are substantially different, the modification does not result in derecognition. Based on the change in cash flows discounted at the original EIR, the Bank records a modification gain or loss, presented within interest revenue calculated using EIR in the statement of profit or loss, to the extent that an impairment loss has not already been recorded.

For modifications not resulting in derecognition, the Bank also reassesses whether here has been a significant increase in credit risk or whether the assets should be classified as credit-impaired. Asset that has been classified as credit-impaired as the result of modification, can be recorded as Stage 2 or Stage 3 if certain criteria are met according to the Banks approved methodology.

Impairment of financial assets under IAS 39

Before 1 January 2018, the Bank assessed at each reporting date whether there was any objective evidence that a financial asset or a group of financial assets was impaired. A financial asset or a group of financial assets was deemed to be impaired if, and only if, there was objective evidence of impairment as a result of one or more events that had occurred after the initial recognition of the asset (an incurred “loss event”) and that loss event (or events) had an impact on the estimated future cash flows of the financial asset or the group of financial assets that could be reliably estimated. Evidence of impairment may have included indications that the borrower or a group of borrowers was experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they would enter bankruptcy or other financial reorganisation and where observable data indicated that there was a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlated with defaults.

The Bank assessed whether objective evidence of impairment existed individually for financial assets that were individually significant, or collectively for financial assets that were not individually significant.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Impairment of financial assets under IAS 39 (continued)

If there was an objective evidence that an impairment loss had been incurred, the amount of the loss was measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred), discounted using original effective interest rate. The carrying amount of the asset was reduced and the amount of the loss was recognised in profit or loss. Interest revenue continued to be accrued on the reduced carrying amount based on the original effective interest rate of the asset. Assets together with the associated allowance were written off when there is no realistic prospect of future recovery and all collateral had been realised or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss decreased because of an event occurring after the impairment had been recognised, the previously recognised impairment loss was reversed in statement of profit or loss.

Information on impairment assessment under IFRS 9 is presented in Note 19.

Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Bank has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; and
- the Bank either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Bank has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Write-off

From 1 January 2018, financial assets are written off either partially or in their entirety only when the Bank has stopped pursuing the recovery. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense. A write-off constitutes a derecognition event.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the National Bank of Georgia, excluding mandatory reserves, and amounts due from credit institutions that mature within ninety days of the date of origination and are free from contractual encumbrances.

Mandatory reserve deposit with the NBG

Mandatory reserve deposits with the NBG are carried at amortised cost and represent interest bearing mandatory reserve deposits which are not available to finance the Bank’s day to day operations and hence are not considered as part of cash and cash equivalents for the purposes of the statement of cash flows. Mandatory reserve is included in amounts due from credit institutions.

Leases

Operating − Bank as lessee

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included into other operating expenses.

Finance − Bank as lessee

The Bank recognises finance leases as assets and liabilities in the statement of financial position at the date of commencement of the lease term at amounts equal to the fair value of the leased property or, if lower, at the present value of the minimum lease payments. In calculating the present value of the minimum lease payments the discount factor used is the interest rate implicit in the lease, when it is practicable to determine; otherwise, the Bank’s incremental borrowing rate is used. Initial direct costs incurred are included as part of the asset. Lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to periods during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount is reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. The right of set-off must not be contingent on a future event and must be legally enforceable in all of the following circumstances:

- the normal course of business;
- the event of default; and
- the event of insolvency or bankruptcy of the entity and all of the counterparties.

These conditions are not generally met in master netting agreements, and the related assets and liabilities are presented gross in the statement of financial position.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Taxation

The current income tax expense is calculated in accordance with the regulations of Georgia.

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (applicable to undistributed profits) and tax laws, that have been enacted or substantively enacted by the end of the reporting period.

Georgia also has various operating taxes that are assessed on the Bank’s activities. These taxes are included as a component of other operating expenses.

Property and equipment

Property and equipment are carried at cost, excluding the costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Depreciation of an asset begins when it is available for use. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	Years
Furniture and fixtures	4
Computers and equipment	4
Motor vehicles	4
Other equipment	5
Leasehold improvements	4

The asset’s residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year-end.

Costs related to repairs and renewals are charged when incurred and included in other operating expenses, unless they qualify for capitalization.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Intangible assets

Intangible assets include computer software and licenses. Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic lives of 10 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets with indefinite useful lives are reviewed at least at each financial year-end.

Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of obligation can be made.

Contingencies

Contingent liabilities are not recognised in the statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the statement of financial position but disclosed when an inflow of economic benefits is probable.

Share capital

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as additional paid-in capital.

Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Interest and similar income and expense

From 1 January 2018, the Bank calculates interest revenue on debt financial assets measured at amortized cost by applying the EIR to the gross carrying amount of financial assets other than credit-impaired assets (before 1 January 2018: by applying EIR to the amortized cost of financial assets). EIR is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest revenue or expense.

When a financial asset becomes credit-impaired, the Bank calculates interest revenue by applying the effective interest rate to the net amortised cost of the financial asset. If the financial assets cures and is no longer credit-impaired, the Bank reverts to calculating interest revenue on a gross basis.

Interest revenue on all financial assets at FVPL is recognised using the contractual interest rate.

3. Summary of accounting policies (continued)

Recognition of income and expenses (continued)

Fee and commission income

The Bank earns fee and commission income from several types of services it provides to its customers. Fee income can be divided into the following categories:

- *Fee income earned from services that are provided over a certain period of time*

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income on guarantees and letters of credit. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the effective interest rate on the loan.

- *Fee income earned at a point in time*

Fees arising from settlement and cash operations are recognized upon completion of the underlying transactions. Each cash operation and settlement operation is treated as a separate performance obligation.

- *Fee income from providing transaction services*

Fees arising from negotiating or participating in the negotiation of a transaction for a third party – such as where the Bank's performance obligation is the arrangement of the acquisition of shares or other securities – are recognised on completion of the underlying transaction. Fees or components of fees that are linked to certain performance obligations are recognised after fulfilling the corresponding criteria. When the contract provides for a variable consideration, fee and commission income is only recognized to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur until the uncertainty associated with the variable consideration is subsequently resolved.

Foreign currency translation

The financial statements are presented in Georgian lari ("GEL"), which is the Bank's functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are recognised in the statement of profit or loss as gains less losses from foreign currencies – translation differences. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Differences between the contractual exchange rate of a transaction in a foreign currency and the NBG exchange rate on the date of the transaction are included in gains less losses from dealing in foreign currencies. The official GEL exchange rates at 31 December 2018 and 2017 were 2.6766 GEL and 2.5922 GEL to 1 USD, respectively, 3.0701 GEL and 3.1044 GEL to 1 EUR, respectively and 1.5786GEL and 1.5249 GEL to 1 AZN, respectively.

(Amounts in tables are in thousands of Georgian lari)

3. Summary of accounting policies (continued)

Standards issued but not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Bank's financial statements which may have impact on the Bank's financial statements are disclosed below. The Bank intends to adopt these standards and interpretations, when they become effective. Management does not expect application of other new standards and interpretations to have significant impact on financial statements.

IFRS 16 Leases

IFRS 16 was issued in January 2016 and it replaces IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement Contains a Lease*, SIC-15 *Operating Leases – Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.

Lessees will be also required to remeasure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset.

Lessor accounting under IFRS 16 is substantially unchanged from today's accounting under IAS 17. Lessors will continue to classify all leases using the same classification principle as in IAS 17 and distinguish between two types of leases: operating and finance leases.

IFRS 16, which is effective for annual periods beginning on or after 1 January 2019, requires lessees and lessors to make more extensive disclosures than under IAS 17.

The Bank plans to adopt IFRS 16 retrospectively with the cumulative effect of initially applying IFRS 16 recognised at the date of initial application. The Bank will elect to apply the standard to contracts that were previously identified as leases applying IAS 17 and IFRIC 4. The Bank will therefore not apply the standard to contracts that were not previously identified as containing a lease applying IAS 17 and IFRIC 4.

The Bank will elect to use the exemptions proposed by the standard on lease contracts for which the lease terms ends within 12 months as of the date of initial application, and lease contracts for which the underlying asset is of low value. The Bank is currently under the process of assessing effect of the IFRS 16.

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

IFRIC Interpretation 23 Uncertainty over Income Tax Treatment

The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12 and does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The Interpretation specifically addresses the following:

- whether an entity considers uncertain tax treatments separately;
- the assumptions an entity makes about the examination of tax treatments by taxation authorities;
- how an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates;
- how an entity considers changes in facts and circumstances.

An entity has to determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments. The approach that better predicts the resolution of the uncertainty should be followed. The interpretation is effective for annual reporting periods beginning on or after 1 January 2019, but certain transition reliefs are available. The Bank will apply the interpretation from its effective date. The Bank does not expect any impact on its financial statements from application of this interpretation.

Amendments to IFRS 9: Prepayment Features with Negative Compensation

Under IFRS 9, a debt instrument can be measured at amortised cost or at fair value through other comprehensive income, provided that the contractual cash flows are 'solely payments of principal and interest on the principal amount outstanding' (the SPPI criterion) and the instrument is held within the appropriate business model for that classification. The amendments to IFRS 9 clarify that a financial asset passes the SPPI criterion regardless of the event or circumstance that causes the early termination of the contract and irrespective of which party pays or receives reasonable compensation for the early termination of the contract.

The amendments should be applied retrospectively and are effective from 1 January 2019, with earlier application permitted. These amendments will have no material impact on the financial statements of the Bank.

Annual Improvements 2015-2017 Cycle (issued in December 2017) include:

IAS 12 Income Taxes

The amendments clarify that the income tax consequences of dividends are linked more directly to past transactions or events that generated distributable profits than to distributions to owners. Therefore, an entity recognises the income tax consequences of dividends in profit or loss, other comprehensive income or equity according to where the entity originally recognised those past transactions or events.

An entity applies those amendments for annual reporting periods beginning on or after 1 January 2019, with early application is permitted. When an entity first applies those amendments, it applies them to the income tax consequences of dividends recognised on or after the beginning of the earliest comparative period. Since the Bank's current practice is in line with these amendments, the Bank does not expect any effect on its financial statements.

(Amounts in tables are in thousands of Georgian lari)

4. Significant accounting judgments and estimates

Estimation uncertainty

In the process of applying the Bank's accounting policies, management has used its judgments and made estimates in determining the amounts recognized in the financial statements. The most significant use of judgments and estimates are as follows:

Impairment losses on financial assets

The measurement of impairment losses both under IFRS 9 and IAS 39 across all categories of financial assets requires judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances. The Bank's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- the Bank's internal credit grading model, which assigns PDs to the individual grades;
- the Bank's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a LTECL basis;
- the segmentation of financial assets when their ECL is assessed on a collective basis;
- development of ECL models, including the various formulae and the choice of inputs;
- determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs;
- selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models.

The amount of allowance for loans to customers and investment securities recognized in the statement of financial position at 31 December 2018 was GEL 2,413 thousand (2017: GEL thousand 3,098 measured under IAS 39) and GEL 242 thousand (2017: GEL 246 thousand measured under IAS 39) respectively (Note 19).

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded in the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. Additional details are provided in Note 20.

(Amounts in tables are in thousands of Georgian lari)

5. Cash and cash equivalents

Cash and cash equivalents comprise:

	2018	2017
Cash on hand	1,225	673
Current accounts with the NBG	398	714
Current accounts with other credit institutions	8,237	13,253
Time deposits with credit institutions up to 90 days	36,643	29,268
Cash and cash equivalents	**46,503**	**43,908**

As at 31 December 2018, current accounts and time deposit accounts with credit institutions denominated in GEL, EUR and USD represent 43.75%, 29.72% and 26.34% of total current and time deposit accounts respectively (31 December 2017: GEL 40.68%, EUR 4.50%, USD 54.12%).

All balances of cash equivalents are allocated to Stage 1. The ECL relating to cash equivalents of the Bank equals nil.

6. Amounts due from credit institutions

Amounts due from credit institutions comprise:

	2018	2017
Mandatory reserve with the NBG	43,001	28,803
Time deposits for more than 90 days	20,395	22,642
Less – allowance for impairment	(291)	–
Amounts due from credit institutions	**63,105**	**51,445**

In 2018 the credit institutions are required to maintain a mandatory interest earning cash deposit with the NBG at the level of 5% and 25% (2017: 7% and 20%) of the average of funds attracted from customers and non-resident financial institutions for the appropriate two-week period in GEL and foreign currencies, respectively.

Time deposits comprise of deposits in USD and GEL placed with resident commercial banks with maturities ranging from May 2019 to July 2019 (31 December 2017: deposits in USD and GEL placed with resident commercial banks with maturities ranging from January 2018 to June 2018).

An analysis of changes in the gross carrying value and corresponding ECL in relation to time deposits for more than 90 days during the year ended 31 December 2018 is as follows:

	Gross caring value	ECL
As at 1 January 2018	**22,642**	**(49)**
New assets originated	31,986	(263)
Assets repaid	(35,016)	288
Foreign exchange and other movements	783	(267)
At 31 December 2018	**20,395**	**(291)**

(Amounts in tables are in thousands of Georgian lari)

7. Loans to customers

Loans to customers comprise:

	2018	2017
Corporate	163,285	114,133
Commercial	27,121	–
Consumer	841	644
Loans to customers	**191,247**	**114,777**
Less – allowance for impairment	(2,413)	(3,098)
Loans to customers	**188,834**	**111,679**

Commercial loans include loans to medium sized companies with annual revenue ranging from GEL 1,500 thousand to GEL 10,000 thousand. The Bank initiated issuance of commercial loans in 2018.

An analysis of changes in the gross carrying value in relation to loans to customers during the year ended 31 December 2018 is as follows:

	Corporate	Commercial	Consumer	Total
Gross carrying value as at 1 January 2018	**114,133**	**–**	**644**	**114,777**
New assets originated	226,105	29,883	1,195	257,183
Assets repaid	(179,368)	(3,050)	(998)	(183,416)
Amounts written off	(1,722)	–	–	(1,722)
Foreign exchange and other movements	4,137	288	–	4,425
At 31 December 2018	**163,285**	**27,121**	**841**	**191,247**

All balances of loans to customers are allocated to stage 1.

An analysis of changes in the ECL allowances during the year ended 31 December 2018 is as follows:

	Corporate	Commercial	Consumer	Total
ECL as at 1 January 2018	**(2,221)**	**–**	**(81)**	**(2,302)**
New assets originated	(3,509)	(241)	(136)	(3,886)
Assets repaid	2,784	25	132	2,941
Amounts written off	1,722	–	–	1,722
Foreign exchange and other movements	(667)	(221)	–	(888)
At 31 December 2018	**(1,891)**	**(437)**	**(85)**	**(2,413)**

(Amounts in tables are in thousands of Georgian lari)

7. Loans to customers (continued)

Comparative amounts of allowance for impairment for the year ended 31 December 2017 represent allowance account for credit losses and reflect measurement basis under IAS 39.

	2017		
	Corporate	**Consumer**	**Total**
At 1 January 2017	**2,049**	**71**	**2,120**
Charge for the year	968	10	978
At 31 December 2017	**3,017**	**81**	**3,098**
Collective impairment	1,301	5	**1,306**
Individual impairment	1,716	76	**1,792**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	9,500	76	**9,576**

Collateral and other credit enhancements

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters. The main types of collateral obtained are charges over real estate properties and guarantees from the Parent.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for loan impairment.

Concentration of loans to customers

As at 31 December 2018, the Bank had a concentration of loans due from three major group of borrowers in the total exposure of GEL 82,188 thousand that represented 42.97% of the total gross loan portfolio (31 December 2017: GEL 61,621 thousands with 53.69% of the gross loan portfolio). An allowance of GEL 639 thousand (31 December 2017: an allowance of GEL 1,957 thousand measured under IAS 39) was recognised against these loans.

Loans are made within Georgia in the following industry sectors:

	2018	**2017**
Trade and services	103,442	53,134
Non-banking credit organizations	59,158	23,652
Transportation and telecommunication	14,765	–
Energy	6,343	16,425
Construction	5,208	12,596
Individuals	841	644
Mining	775	4,611
Other	715	3,715
	191,247	**114,777**

(Amounts in tables are in thousands of Georgian lari)

8. Investment securities

As at 31 December 2018, investment securities comprised of debt securities of companies and commercial banks registered in Georgia.

Investment securities comprise:

	2018	2017
Debt securities at amortised cost (previously classified as loans and receivables)		
Corporate bonds	18,566	12,177
Bonds of financial institutions	1,902	22,079
Certificates of deposit of financial institutions	–	26,849
Treasury bonds of the Ministry of Finance of Georgia	–	1,174
	20,468	**62,279**
Less: allowance for impairment	(242)	(246)
Total debt securities	**20,226**	**62,033**

An analysis of changes in the gross carrying value in relation to investment securities during the year ended 31 December 2018 is as follows:

	Corporate bonds	Bonds of financial institutions	Certificates of deposit of financial institutions	Treasury bonds of the Ministry of Finance of Georgia	Total
Gross carrying value as at 1 January 2018	**12,177**	**22,079**	**26,849**	**1,174**	**62,279**
New assets originated	6,226	–	–	–	**6,226**
Assets repaid	(15)	(20,000)	(26,574)	(1,174)	**(47,763)**
Foreign exchange and other movements	178	(177)	(275)	–	**(274)**
At 31 December 2018	**18,566**	**1,902**	**–**	**–**	**20,468**

An analysis of changes in the ECL allowances during the year ended 31 December 2018 is as follows:

	Corporate bonds	Bonds of financial institutions	Certificates of deposit of financial institutions	Total
ECL as at 1 January 2018	**(27)**	**(793)**	**(45)**	**(865)**
New assets originated	(176)	–	–	**(176)**
Assets repaid	–	754	111	**865**
Foreign exchange and other movements	–	–	(66)	**(66)**
At 31 December 2018	**(203)**	**(39)**	**–**	**(242)**

All balances of investment securities are allocated to stage 1.

(Amounts in tables are in thousands of Georgian lari)

9. Property and equipment

The movements in property and equipment were as follows:

	Furniture and fixtures	Computers and equipment	Motor vehicles	Other equipment	Leasehold improve-ments	Total
Cost						
1 January 2017	**1,843**	**2,412**	**313**	**486**	**1,912**	**6,966**
Additions	9	607	135	11	4	766
Disposals	–	(6)	(68)	–	–	(74)
31 December 2017	**1,852**	**3,013**	**380**	**497**	**1,916**	**7,658**
Additions	278	915	192	85	154	1,624
Disposals and write-offs	–	(10)	(47)	(3)	–	(60)
31 December 2018	**2,130**	**3,918**	**525**	**579**	**2,070**	**9,222**
Accumulated depreciation						
1 January 2017	**(1,634)**	**(2,052)**	**(185)**	**(327)**	**(1,660)**	**(5,858)**
Depreciation charge	(193)	(348)	(72)	(98)	(252)	(963)
Disposals and write-offs	–	1	68	–	–	69
31 December 2017	**(1,827)**	**(2,399)**	**(189)**	**(425)**	**(1,912)**	**(6,752)**
Depreciation charge	(19)	(220)	(105)	(45)	(5)	(394)
Disposals and write-offs	–	10	47	3	–	60
31 December 2018	**(1,846)**	**(2,609)**	**(247)**	**(467)**	**(1,917)**	**(7,086)**
Net book value						
1 January 2017	**209**	**360**	**128**	**159**	**252**	**1,108**
31 December 2017	**25**	**614**	**191**	**72**	**4**	**906**
31 December 2018	**284**	**1,309**	**278**	**112**	**153**	**2,136**

(Amounts in tables are in thousands of Georgian lari)

10. Intangible assets

The movements in intangible assets were as follows:

	Licenses	Computer software	Total
Cost			
1 January 2017	**897**	**1,829**	**2,726**
Additions	284	166	450
Disposals and write offs	(192)	(2)	(194)
31 December 2017	**989**	**1,993**	**2,982**
Internal transfer	(838)	838	–
Additions	–	951	951
Disposals and write offs	–	(167)	(167)
31 December 2018	**151**	**3,615**	**3,766**
Accumulated amortization			
1 January 2017	**(308)**	**(358)**	**(666)**
Amortisation charge	(204)	(184)	(388)
Disposals and write offs	192	2	194
31 December 2017	**(320)**	**(540)**	**(860)**
Internal transfer	260	(260)	–
Amortisation charge	(17)	(541)	(558)
Disposals and write offs	–	165	165
31 December 2018	**(77)**	**(1,176)**	**(1,253)**
Net book value			
1 January 2017	**589**	**1,471**	**2,060**
31 December 2017	**669**	**1,453**	**2,122**
31 December 2018	**74**	**2,439**	**2,513**

11. Other assets and liabilities

Other assets comprise:

	2018	2017
Other non-financial assets		
Prepayments for operating lease	1,270	218
Prepayments for acquisition of property plant and equipment and intangible assets	1,144	4
Prepaid expenses	614	362
Inventory	107	37
Prepaid taxes other than income tax	3	10
Other	39	18
	3,177	**649**
Other financial assets		
Derivative financial assets	415	62
	415	**62**
Total other assets	**3,592**	**711**

(Amounts in tables are in thousands of Georgian lari)

11. Other assets and liabilities (continued)

The table below shows the fair values of derivative financial instruments, recorded as assets, together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying asset or liability and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of the credit risk.

	2018			*2017*		
	Notional	*Fair values*		*Notional*	*Fair value*	
	amount	*Asset*	*Liability*	*amount*	*Asset*	*Liability*
Interest rate contracts						
Forwards – foreign	12,499	–	23	–	–	–
Forwards – domestic	26,212	415	46	2,592	62	–
Total derivative assets/liabilities		**415**	**69**		**62**	**–**

Foreign and domestic in the table above stand for counterparties where foreign means non-Georgian entities and domestic means Georgian entities.

Other liabilities comprise:

	2018	**2017**
Other financial liabilities		
Other financial liabilities	320	131
Derivative financial liabilities	69	–
	389	**131**
Other non-financial liabilities		
Payable to employees	1,524	1,111
Deferred income	23	36
Taxes other than income tax	4	1
	1,551	**1,148**
Total other liabilities	**1,940**	**1,279**

12. Amounts due to credit institutions

Amounts due to credit institutions comprise:

	2018	**2017**
Time deposits of non-resident commercial banks	95,168	27,122
Time deposits of the Parent	7,766	52,069
Time deposits of resident commercial banks	7,009	22,688
Overdraft from the Parent	202	10
Current accounts of the Parent	117	1,511
Short-term loan from the NBG	–	3,002
Amounts due to credit institutions	**110,262**	**106,402**

As at 31 December 2018 the time deposits of non-resident commercial banks are comprised of USD denominated deposits of an entity under common control and other non-resident banks (2017: USD and EUR denominated deposits of an entity under common control and other non-resident bank).

As at 31 December 2018 time deposits of resident commercial banks comprise of deposits placed by a single resident commercial bank, are denominated in GEL and mature in January 2019 (2017: time deposits placed by three resident commercial banks were denominated in GEL and EUR and matured in January and February 2018).

(Amounts in tables are in thousands of Georgian lari)

13. Amounts due to customers

The amounts due to customers include the following:

	2018	2017
Current and demand accounts	60,249	19,233
Time deposits	44,290	38,948
Amounts due to customers	**104,539**	**58,181**
Held as security against guarantees issued (Note 16)	8,896	4,342

As at 31 December 2018, amounts due to customers included balances with three major customers of GEL 37,101 thousand that constituted 35.49% of the total of customer accounts (31 December 2017: 28,726 thousand that constituted 49.37% of the total of customer accounts).

An analysis of customer accounts by economic sector follows:

	2018	2017
Trade and service	61,332	27,650
Individuals	20,328	11,016
Construction	6,686	4,816
Insurance	6,638	6,360
Energy	6,431	5,105
Non-banking credit organizations	2,738	3,223
Other	386	11
Amounts due to customers	**104,539**	**58,181**

14. Taxation

In June 2016, amendments to the Georgian tax law in respect of corporate income tax became enacted. The amendments became effective from 1 January 2017 for all Georgian companies except the banks, insurance companies and microfinance organization, for which the effective date was initially set at January 2019. On 5 May 2018 amendment was made in tax code and the date was revised to January 2023. Under the new regulation, corporate income tax will be levied on profit distributed as dividends, rather than on profit earned as under the current regulation. The amount of tax payable on a dividend distribution will be calculated as 15/85 of the amount of net distribution. The companies will be able to offset corporate income tax liability arising from dividend distributions out of profits earned in 2008-2016 by the amount of corporate income tax paid for the respective period under the current regulation. Dividends distributions between Georgian resident companies will not be subject to corporate income tax.

Following the enactment of the latest amendment, the Bank recalculated its deferred tax assets at 31 December 2018 and recognized deferred tax benefit in the profit and loss statement for 2018. As IAS 12 Income Taxes requires, the Bank used 0% tax rate applicable for undistributed profits in respect of assets and liabilities expected to be realized or settled in the periods after January 2023.

The corporate income tax benefit for the year ended 31 December 2018 comprises of deferred tax benefit of GEL 148 thousand (31 December 2017: expense of GEL 924 thousand).

(Amounts in tables are in thousands of Georgian lari)

14. Taxation (continued)

In 2018 and 2017 the income tax rate applicable to the Bank's income is 15%. The effective income tax rate differs from the statutory income tax rate. A reconciliation of the income tax benefit expense on statutory rates with actual is as follows:

	2018	2017
Profit before income tax	**3,041**	**4,377**
Statutory tax rate	15%	15%
Theoretical income tax expense at the statutory rate	**(456)**	**(657)**
Tax exempt income	100	131
Non-deductible expenses	(87)	(3)
Effect from change in tax legislation	229	61
Tax losses utilized during the year	362	(456)
Income tax benefit/(expense)	**148**	**(924)**

Deferred tax assets and liabilities as at 31 December 2018 and 31 December 2017 and their movements for the respective period:

	2016	Through statement of profit and loss	2017	Through statement of profit and loss	2018
Tax effect of deductible temporary differences					
Tax losses carried forward	804	(804)	–	193	193
Property, plant and equipment	226	(226)	–	176	176
Amounts due from credit institutions	–	–	–	44	44
Other liabilities	135	(135)	–	110	110
Deferred tax asset	**1,165**	**(1,165)**	**–**	**523**	**523**
Tax effect of taxable temporary differences					
Investment securities	(12)	12	–	(58)	(58)
Intangible assets	(52)	52	–	(69)	(69)
Loans to customers	(177)	177	–	(248)	(248)
Deferred tax liability	**(241)**	**241**	**–**	**(375)**	**(375)**
Deferred tax asset/(liability)	**924**	**(924)**	**–**	**148**	**148**

The Bank's accumulated tax losses at 31 December 2018 equal GEL 1,285 thousand which begin to expire in 2019 if not utilized.

15. Equity

As at 31 December 2018 and 2017, the Bank's authorized, issued and fully paid capital amounted to GEL 103,000 thousand comprising of 103,000,000 common shares with nominal value of GEL 1 each. Each share entitles one vote to the shareholder.

In accordance with Georgian legislation, dividends may only be declared by the Bank's Parent from the net income as shown in the Bank's financial statements prepared in compliance with the NBG requirements. The Bank is obliged to officially inform the NBG of any dividends declared and the NBG reserves the right to suspend or restrict the disbursement of dividends should the Bank be in breach of the NBG regulations.

No dividends were declared or paid during the year ended 31 December 2018 (2017: nil).

(Amounts in tables are in thousands of Georgian lari)

16. Commitments and contingencies

Taxation

Georgian tax legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Bank may be challenged by the relevant tax authorities. It is possible that transactions and activities that have not been challenged in the past may be challenged in the future. As such, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Management believes that its interpretation of the relevant legislation as at 31 December 2018 is appropriate and that the Bank's tax, currency and customs positions will be sustained.

Commitments and contingencies

As at 31 December 2018 and 2017, the Bank's commitments and contingencies comprised the following:

	2018	2017
Credit related commitments		
Unused credit lines	25,703	23,341
Letters of credit	3,846	1,478
	29,549	**24,819**
Operating lease commitments		
Not later than 1 year	2,097	1,831
More than 1 year but less than 5 years	12,849	6,553
	14,946	**8,384**
Performance guarantees issued		
Performance guarantees issued	31,802	22,566
	31,802	**22,566**
Less: ECL for credit related commitments	(70)	(135)
Commitments and contingencies (before deducting collateral)	**76,227**	**55,634**
Less: deposits held as security against guarantees issued (Note 13)	(8,896)	(4,342)
Commitments and contingencies	**67,331**	**51,292**

An analysis of changes in the ECL allowances during the year ended 31 December 2018 is, as follows:

	Letters of credit	Guarantees	Unused credit lines	Total
ECL as at 1 January 2018	**(1)**	**(12)**	**(4)**	**(17)**
New exposures	(1)	–	(84)	(85)
Matured exposures	–	12	19	31
Foreign exchange and other movements	–	–	1	1
At 31 December 2018	**(2)**	**–**	**(68)**	**(70)**

All balances of guarantees issued and letters of credit are allocated to stage 1.

(Amounts in tables are in thousands of Georgian lari)

17. Net fee and commission income

Net fee and commission income comprise:

	2018	2017
Guarantees and letters of credits issued	513	397
Settlement operations	178	127
Cash operations	84	17
Brokerage operations	20	48
Plastic cards operations	10	5
Currency conversion operations	–	4
Other commission income	–	71
Fee and commission income	**805**	**669**
Settlement operations	(241)	(189)
Plastic card operations	(104)	(108)
Guarantees and letters of credits issued	(66)	(111)
Cash operations	(3)	(5)
Brokerage operations	(1)	(1)
Fee and commission expense	**(415)**	**(414)**
Net fee and commission income	**390**	**255**

Revenue from contracts with customers

The Bank's revenue from contracts with customers is mostly represented by fee and commission income. Revenue from contracts with customers recognized in the statement of profit or loss for the year ended 31 December 2018 amounted to GEL 805 thousand.

The Bank recognised the following contract assets and liabilities in statement of financial position related to its contracts with customers:

	2018	1 January 2018
Deferred income (presented within other liabilities)	23	36

The Bank usually collects fees and commissions in advance of completion of the underlying transaction or shortly thereafter (for contracts where performance obligation is satisfied point in time, such as settlement transactions). For services provided over time (such as those related to fees for guarantees and letters of credit issued), the Bank usually charges upfront monthly, quarterly or annual fees covering respective portion of the overall contract period.

The Bank recognised GEL 36 revenue from contracts with customers in the current reporting period that relates to carried-forward contract liabilities included in deferred income as at 1 January 2018.

(Amounts in tables are in thousands of Georgian lari)

18. Personnel, general and administrative expenses

Personnel, general and administrative expenses comprise:

	2018	2017
Salaries	5,884	3,870
Bonuses and other employee benefits	2,374	1,550
Personnel expenses	**8,258**	**5,420**
Operating leases	2,139	1,679
Professional services	2,040	2,065
Advertising costs	260	469
Personnel training	135	191
Utilities	130	119
Transportation and business trip expenses	124	123
Corporate hospitality and entertainment	119	169
Recruitment costs	82	1
Maintenance and exploitation	79	49
Insurance	66	71
Security expenses	60	58
Membership fees	40	38
Charity costs	18	29
Taxes other than income tax	15	10
Deposit insurance fee	2	100
Communication	–	5
Other	157	126
General and administrative expenses	**5,466**	**5,302**

Remuneration of the Bank's auditor for the years ended 31 December 2018 and 2017 comprises (net of VAT):

	2018	2017
Fees for the audit of the Bank's annual financial statements for the year ended 31 December	105	90
Expenditures for other assurance services	52	38
Expenditures for other professional service	12	1
Total fees and expenditures	**169**	**129**

Fees and expenditures payable to other auditors and audit firms in respect of other professional services comprised GEL 23 thousand (2017: GEL 721 thousand).

(Amounts in tables are in thousands of Georgian lari)

19. Risk management

Introduction

Risk is inherent in the Bank's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Bank's continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The Bank is exposed to credit risk, liquidity risk and market risk, the latter being subdivided into trading and non-trading risks. It is also subject to operating risks.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. They are monitored through the Bank's strategic planning process.

Risk management structure

Board of Directors

The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and principles. The Board of Directors is ultimately responsible for identifying and controlling risks and different departments and committees which are responsible for managing and monitoring risks.

Risk management

The Risk Management Department is responsible for determining, implementing and maintaining risk management framework.

Asset and Liability Committee

Asset and Liability Committee (ALCO) is responsible for managing the Bank's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding, liquidity, interest rate, and capital adequacy risks of the Bank.

Internal Audit

Risk management processes throughout the Bank are audited by the internal audit function on a constant basis, which examines the adequacy of the procedures, their design and operational effectiveness, and the Bank's compliance both with the regulatory requirements and internal procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee.

Audit Committee

The Audit Committee is responsible for the fundamental risk issues and manages and monitors relevant risk decisions and performance of control functions by other departments in the Bank pertaining to general control environment, manual, IT dependent or application controls, intentional or unintentional misstatement risks, risk of fraud or misappropriation of assets, information security, anti-money laundering, etc. Audit committee is comprised of three members, out of which two are independent.

(Amounts in tables are in thousands of Georgian lari)

19. Risk management (continued)

Risk management structure (continued)

Risk measurement and reporting systems

Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the Bank is willing to accept. In addition the Bank monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risk types and activities. The main body to which the risks are reported is ALCO. The respective meetings are held once a month.

Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

Credit risk

Credit risk is the risk that the Bank will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. The Bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and by monitoring exposures in relation to such limits.

The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. The credit quality review process allows the Bank to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

Actual exposure per borrower against limits is monitored on loans granted. The Credit Committee may initiate a change in the limits. Where appropriate, the Bank obtains collateral and corporate guarantees. The credit risks are monitored on a continuous basis and are subject to annual or more frequent reviews.

Credit-related commitments risks

The Bank makes available to its customers guarantees which may require that the Bank make payments on their behalf. Such payments are collected from customers based on the terms of guarantee. They expose the Bank to similar risks to loans and these are mitigated by the same control processes and policies.

(Amounts in tables are in thousands of Georgian lari)

19. Risk management (continued)

Credit risk (continued)

Impairment assessment

From 1 January 2018, the Bank calculates ECL based on several probability-weighted scenarios to measure the expected cash shortfalls, discounted at an approximation to the EIR. A cash shortfall is the difference between the cash flows that are due to the Bank in accordance with the contract and the cash flows that the entity expects to receive. The mechanics of the ECL calculations are outlined below and the key elements are as follows:

PD	The *Probability of Default* is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio.
EAD	The *Exposure at Default* is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest from missed payments.
LGD	The *Loss Given Default* is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from the realisation of any collateral. It is usually expressed as a percentage of the EAD.

The ECL allowance is based on the 12 months' expected credit loss (12mECL), unless there has been significant increase in credit risk since origination or other impairment indicators were identified, in which case the ECL allowance is based on the credit losses expected to arise over the life of the asset (the lifetime expected credit loss or LTECL). The 12mECL is the portion of LTECL that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Both LTECL and 12mECL are calculated on either an individual basis or a collective basis, depending on the nature of the underlying portfolio of financial instruments.

The Bank has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument. Based on the above process, the Bank groups its loans into Stage 1, Stage 2, Stage 3 and POCI, as described below:

Stage 1:	When loans are first recognised, the Bank recognises an allowance based on 12mECL. Stage 1 loans also include facilities where the credit risk has improved and the loan has been reclassified from Stage 2.
Stage 2:	When a loan has shown a significant increase in credit risk since origination, the Bank records an allowance for the LTECL. Stage 2 loans also include facilities, where the credit risk has improved and the loan has been reclassified from Stage 3.
Stage 3:	Loans considered credit-impaired. The Bank records an allowance for the LTECL.
POCI:	Purchased or originated credit impaired (POCI) assets are financial assets that are credit impaired on initial recognition. POCI assets are recorded at fair value at original recognition and interest revenue is subsequently recognised based on a credit-adjusted EIR. ECL are only recognised or released to the extent that there is a subsequent change in the lifetime expected credit losses.

19. Risk management (continued)

Credit risk (continued)

Definition of default and cure

The Bank considers a financial instrument defaulted and therefore Stage 3 (credit-impaired) for ECL calculations in all cases when the borrower becomes 90 days past due on its contractual payments. The Bank considers amounts due from banks defaulted and takes immediate action when the required intraday payments are not settled by the close of business as outlined in the individual agreements.

As a part of a qualitative assessment of whether a customer is in default, the Bank also considers a variety of instances that may indicate unlikeliness to pay. When such events occur, the Bank carefully considers whether the event should result in treating the customer as defaulted and therefore assessed as Stage 3 for ECL calculations or whether Stage 2 is appropriate.

The Bank has defined certain criteria which should be met in order to consider asset as cured. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition.

Internal rating and PD estimation process

The Bank's Credit Risk Department operates its internal rating models. The Bank runs separate models for its key portfolios in which its customers are rated from Aaa to Ca-C using internal grades. The models incorporate both qualitative and quantitative information and, in addition to information specific to the borrower, utilize supplemental external information that could affect the borrower's behavior. Where practical, they also build on information from the national and international external rating agencies. PDs, incorporating forward looking information and the IFRS 9 stage classification of the exposure, are assigned for each grade. This is repeated for each economic scenario as appropriate.

Treasury and interbank relationships

The Bank's treasury and interbank relationships and counterparties comprise financial services institutions, banks. For these relationships, the Bank's credit risk department analyses publicly available information such as financial information and other external data, e.g., the external ratings, and assigns the internal rating, as shown in the table below.

Corporate and commercial lending

For corporate and commercial loans, the borrowers are assessed by specialised credit risk employees of the Bank. The credit risk assessment is based on a credit scoring model that takes into account various historical, current and forward-looking information such as:

- historical financial information together with forecasts and budgets prepared by the client. This financial information includes realised and expected results, solvency ratios, liquidity ratios and any other relevant ratios to measure the client's financial performance. Some of these indicators are captured in covenants with the clients and are, therefore, measured with greater attention;
- any publicly available information on the clients from external parties. This includes external rating grades issued by rating agencies, independent analyst reports, publicly traded bond prices or press releases and articles;
- any macro-economic or geopolitical information, e.g., GDP growth relevant for the specific industry and geographical segments where the client operates;
- any other objectively supportable information on the quality and abilities of the client's management relevant for the company's performance.

(Amounts in tables are in thousands of Georgian lari)

19. Risk management (continued)

Credit risk (continued)

Consumer lending

Consumer lending comprises of employee loans and overdrafts. Credit risk and relevant loan loss allowance on this portfolio is assessed on a collective basis for performing loans and individual basis in relation to non-performing loans.

The Bank's internal credit rating grades are as follows:

Internal rating Grade	Internal rating	Lifetime PD	Internal rating description
Class 1	Aaa	0.24%	High grade
Class 1	Aa1	0.26%	High grade
Class 1	Aa2	0.29%	High grade
Class 1	Aa3	0.32%	High grade
Class 1	A1	0.35%	High grade
Class 1	A2	0.39%	High grade
Class 1	A3	0.44%	High grade
Class 1	Baa1	0.50%	Standard grade
Class 1	Baa2	0.57%	Standard grade
Class 1	Baa3	0.66%	Standard grade
Class 1	Ba1	0.78%	Standard grade
Class 1	Ba2	0.94%	Standard grade
Class 1	Ba3	1.17%	Standard grade
Class 2	B1	1.52%	Standard grade
Class 2	B2	2.13%	Standard grade
Class 3	B3	3.29%	Standard grade
Class 3	Caa1	5.71%	Sub-standard grade
Class 3	Caa2	11.26%	Sub-standard grade
Class 3	Caa3	25.34%	Sub-standard grade
Class 3	Ca-C	30.12%	Sub-standard grade
	Default	100%	Impaired

Exposure at default

The exposure at default (EAD) represents the gross carrying amount of the financial instruments subject to the impairment calculation, addressing both the client's ability to increase its exposure while approaching default and potential early repayments too. To calculate the EAD for a Stage 1 loan, the Bank assesses the possible default events within 12 months for the calculation of the 12mECL. For Stage 2, Stage 3 and POCI financial assets, the exposure at default is considered for events over the lifetime of the instruments.

Loss given default

The credit risk assessment is based on a standardised LGD assessment framework that results in a certain LGD rate. These LGD rates take into account the expected EAD in comparison to the amount expected to be recovered or realised from any collateral held.

19. Risk management (continued)

Credit risk (continued)

Significant increase in credit risk

The Bank continuously monitors all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12mECL or LTECL, the Bank assesses whether there has been a significant increase in credit risk since initial recognition.

The Bank also applies a secondary qualitative method for triggering a significant increase in credit risk for an asset, such as moving a customer/facility to the watch list, or the account becoming restructured due to credit event. Regardless of the change in credit grades, if contractual payments are more than 30 days past due, the credit risk is deemed to have increased significantly since initial recognition.

When estimating ECLs on a collective basis for a group of similar assets, the Bank applies the same principles for assessing whether there has been a significant increase in credit risk since initial recognition.

Grouping financial assets measured on a collective basis

Dependent on the factors below, the Bank calculates ECLs either on a collective or on an individual basis.

Asset classes where the Bank calculates ECL on an individual basis include:

- all Stage 3 assets, regardless of the class of financial assets;
- Stage 2 and Stage 3 corporatel and commercial portfolio;
- exposures that have been classified as POCI when the original loan was derecognised and a new loan was recognised as a result of a credit driven debt restructuring.

Asset classes where the Bank calculates ECL on a collective basis include:

- the smaller and more generic balances of the Bank's commercial portfolio;
- Stage 1 and 2 consumer lending;

The Bank groups these exposures into smaller homogeneous portfolios, based on a combination of internal and external characteristics of the loans, for example internal grade, overdue bucket, product type, or borrower's industry.

Forward-looking information and multiple economic scenarios

In its ECL models, the Bank relies on a range of forward looking information as economic inputs, such as:

- GDP growth;
- unemployment rates;
- foreign exchange rates.

The inputs and models used for calculating ECLs may not always capture all characteristics of the market at the date of the financial statements. To reflect this, qualitative adjustments or overlays are occasionally made as temporary adjustments when such differences are significantly material.

(Amounts in tables are in thousands of Georgian lari)

19. Risk management (continued)

Credit risk (continued)

The Bank obtains the forward-looking information from the sources published by the NBG. Experts of the Bank's Credit Risk Department determine the weights attributable to the multiple scenarios. The tables show the values of the key forward looking economic variables/assumptions used in each of the economic scenarios for the ECL calculations. The figures for "Subsequent years" represent a long-term average and so are the same for each scenario as at 31 December 2018.

Key drivers	ECL scenario	Assigned probabilities, %
GDP growth, %		
	Upside	25%
	Base case	50%
	Downside	25%
USD/GEL exchange rate		
	Upside	25%
	Base case	50%
	Downside	25%
Unemployment rate, %		
	Upside	25%
	Base case	50%
	Downside	25%

Credit quality per class of financial asset

The credit quality of financial assets is managed by the Bank internal credit ratings, as described above. As at 31 December 2018 all financial assets of the Bank are classified as Stage 1. The table below shows the credit quality by class of financial assets, based on the Bank's credit rating system updated:

	Note	High grade	Standard grade	Sub-standard grade	Total
Cash and cash equivalents, except for cash on hand	5	1,772	43,506	–	**45,278**
Amounts due from credit institutions	6	–	58,083	5,313	**63,396**
Loans to customers at amortised cost	7				
Corporate		–	151,356	11,929	**163,285**
Commercial		–	22,618	4,503	**27,121**
Consumer		–	841	–	**841**
Debt investment securities at amortized cost	8	–	20,468	–	**20,468**
Unused credit lines	16	–	23,114	2,589	**25,703**
Letters of credit	16	–	3,846	–	**3,846**
Total		**1,772**	**323,832**	**24,334**	**349,938**

(Amounts in tables are in thousands of Georgian lari)

19. Risk management (continued)

Credit risk (continued)

The table below shows gross balances under IAS 39 as at 31 December 2017 based on the Bank's internal credit rating system:

	Notes	High grade 2017	Individually impaired	Total 2017
Amounts due from credit institutions	6	51,445	–	**51,445**
Loans to customers	7	105,201	9,576	**114,777**
Investment securities	8	62,279	–	**62,279**
Total		**218,925**	**9,576**	**228,501**

The geographical concentration of Bank's financial assets and liabilities is set out below:

	2018				2017			
	Georgia	OECD	Other Non-OECD	Total	Georgia	OECD	Other Non-OECD	Total
Assets								
Cash and cash equivalents	43,384	1,797	1,322	**46,503**	35,380	6,474	2,054	**43,908**
Amounts due from credit institutions	63,105	–	–	**63,105**	51,445	–	–	**51,445**
Loans to customers	188,834	–	–	**188,834**	111,679	–	–	**111,679**
Investment securities	20,226	–	–	**20,226**	62,033	–	–	**62,033**
Other assets	415	–	–	**415**	62	–	–	**62**
	315,964	**1,797**	**1,322**	**319,083**	**260,599**	**6,474**	**2,054**	**269,127**
Liabilities								
Amounts due to credit institutions	7,009	–	103,253	**110,262**	25,690	–	80,712	**106,402**
Amounts due to customers	78,375	2,686	23,478	**104,539**	41,081	–	17,100	**58,181**
Other liabilities	196	69	124	**389**	131	–	–	**131**
	85,580	**2,755**	**126,855**	**215,190**	**66,902**	–	**97,812**	**164,714**
Net assets/(liabilities)	**230,384**	**(958)**	**(125,533)**	**103,893**	**193,697**	**6,474**	**(95,758)**	**104,413**

Liquidity risk and funding management

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. Funds attracted from the Parent provide sufficient sources for the Bank's operations in the foreseeable future. The Bank manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Bank maintains a portfolio of corporate bonds that can be pledged to the NBG in the event of an unforeseen interruption of cash flow. In addition, the Bank maintains a cash deposit (obligatory reserve) with the NBG, the amount of which depends on the level of customer funds attracted.

(Amounts in tables are in thousands of Georgian lari)

19. Risk management (continued)

Liquidity risk and funding management (continued)

The liquidity position is assessed and managed by the Bank primarily on a standalone basis, based on certain liquidity ratios established by the NBG. As at 31 December, these ratios were as follows:

	2018,%	2017,%
LK "Average Liquidity Ratio" (Average volume of liquid assets / Average volume of liabilities)	34.45	47.41

Analysis of financial liabilities by remaining contractual maturities

The tables below summarize the maturity profile of the Bank's financial liabilities at 31 December based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

As at 31 December 2018	**Less than 3 months**	**3 to 12 months**	**1 to 5 years**	**Total**
Financial liabilities				
Amounts due to credit institutions	20,579	59,117	34,189	**113,885**
Amounts due to customers	80,901	24,054	336	**105,291**
Other financial liabilities	389	–	–	**389**
Total undiscounted financial liabilities	**101,869**	**83,171**	**34,525**	**219,565**

As at 31 December 2017	**Less than 3 months**	**3 to 12 months**	**1 to 5 years**	**Total**
Financial liabilities				
Amounts due to credit institutions	67,309	40,420	–	**107,729**
Amounts due to customers	37,674	16,212	4,682	**58,568**
Other financial liabilities	131	–	–	**131**
Total undiscounted financial liabilities	**105,114**	**56,632**	**4,682**	**166,428**

The table below shows the contractual expiry by maturity of the Bank's financial commitments and contingencies. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down.

	Note	**Less than 3 months**	**1 to 5 years**	**Over 5 years**	**Total**
2018	16	29,549	–	–	**29,549**
2017	16	24,819	–	–	**24,819**

The Bank expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments. The maturity analysis does not reflect the historical stability of current accounts. Their liquidation has historically taken place over a longer period than indicated in the table above. These balances are included in amounts due in less than three months in the tables above.

(Amounts in tables are in thousands of Georgian lari)

19. Risk management (continued)

Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchanges, and equity prices. Except for the concentrations within foreign currency, the Bank has no significant concentration of market risk.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank has set limits on positions by currency based on the NBG regulations. Positions are monitored on a daily basis.

The tables below indicate the currencies to which the Bank had significant exposure at 31 December on its monetary assets and liabilities. The analysis calculates the effect of a reasonably possible movement of the currency rate against the GEL, with all other variables held constant on the statement of profit or loss. The effect on equity does not differ from the effect on the statement of profit or loss. A negative amount in the table reflects a potential net reduction in the statement of profit or loss or equity, while a positive amount reflects a net potential increase.

Currency	**Change in currency rate 2018**	**Effect on profit before tax 2018**	**Change in currency rate 2017**	**Effect on profit before tax 2017**
USD	15%/(15%)	1,195/(1,195)	15%/(15%)	261/(261)
EUR	15%/(15%)	(70)/70	15%/(15%)	(19)/19

Prepayment risk

Prepayment risk is the risk that the Bank will incur a financial loss because its customers and counterparties repay or request repayment earlier or later than expected.

The effect on profit before tax for one year assuming 10% of repayable financial instruments were to prepay at the beginning of the year, with all other variables held constant, is as follows:

	Decrease of net interest income
2018	1,837
2017	1,208

(Amounts in tables are in thousands of Georgian lari)

19. Risk management (continued)

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant, of the Bank's statement of profit or loss.

The sensitivity of the statement of profit or loss is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held at 31 December.

Currency	Increase/(decrease) in basis points 2018	Sensitivity of net interest income 2018
GEL	100/(100)	432/(432)

Currency	Increase/(decrease) in basis points 2017	Sensitivity of net interest income 2017
GEL	100/(100)	115/(115)

Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but a control framework and monitoring and responding to potential risks could be effective tools to manage the risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

(Amounts in tables are in thousands of Georgian lari)

20. Fair value measurements

Fair value hierarchy

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

	Fair value measurement using			
At 31 December 2018	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets for which fair values are disclosed				
Cash and cash equivalents	46,503	–	–	**46,503**
Amounts due from credit institutions	–	–	63,105	**63,105**
Loans to customers	–	–	188,834	**188,834**
Investment securities	–	–	20,226	**20,226**
Assets measured at fair value				
Other assets - derivative financial assets	–	415	–	**415**

	Fair value measurement using			
At 31 December 2018	**Level 1**	**Level 2**	**Level 3**	**Total**
Liabilities for which fair values are disclosed				
Amounts due to credit institutions	–	–	110,262	**110,262**
Amounts due to customers	–	–	104,539	**104,539**
Liabilities measured at fair value				
Other liabilities - derivative financial assets	–	69	–	**69**

	Fair value measurement using			
At 31 December 2017	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets for which fair values are disclosed				
Cash and cash equivalents	43,908	–	–	**43,908**
Amounts due from credit institutions	–	–	51,445	**51,445**
Loans to customers	–	–	111,679	**111,679**
Investment securities	–	–	62,033	**62,033**
Assets measured at fair value				
Other assets - derivative financial assets	–	62	–	**62**

	Fair value measurement using			
At 31 December 2017	**Level 1**	**Level 2**	**Level 3**	**Total**
Liabilities for which fair values are disclosed				
Amounts due to credit institutions	–	–	106,402	**106,402**
Amounts due to customers	–	–	58,181	**58,181**

(Amounts in tables are in thousands of Georgian lari)

20. Fair value measurements (continued)

Fair value of financial assets and liabilities not carried at fair value

Set out below is a comparison by class of the carrying amounts and fair values of the Bank's financial instruments that are not carried at fair value in the statement of financial position. The table does not include the fair values of non-financial assets and non-financial liabilities.

	Carrying value 2018	Fair value 2018	Unrecog-nised gain 2018	Carrying value 2017	Fair value 2017	Unrecog-nised gain 2017
Financial assets						
Cash and cash equivalents	46,503	46,503	–	43,908	43,908	–
Amounts due from credit institutions	63,105	63,105	–	51,445	51,445	–
Loans to customers	188,834	188,834	–	111,679	111,679	–
Investment securities	20,226	21,183	957	62,033	63,071	1,038
Other financial assets	415	415	–	62	62	–
Financial liabilities						
Amounts due to credit institutions	110,262	110,262	–	106,402	106,402	–
Amounts due to customers	104,539	104,539	–	58,181	58,181	–
Other financial liabilities	389	389	–	131	131	–
Total unrecognised change in fair value			**957**			**1,038**

Valuation techniques and assumptions

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements.

Assets for which fair value approximates carrying value

For financial assets and financial liabilities that are liquid or having a short term maturity (less than three months) it is assumed that the carrying amounts approximate to their fair value. All of the Bank's financial assets excluding loans to customers and investment securities (i.e. cash and cash equivalents and amounts due from credit institutions) and financial liabilities (amounts due to customers) are either liquid or are maturing within 3 months from the reporting date.

The fair value of loans to customers is estimated by comparing market interest rates when they were first recognized with current market rates offered for similar financial assets. The majority of loans to customers outstanding as at 31 December were issued within 12 months period ended 31 December 2018 at market interest rates, while the contractual interest rates of those loans issued in 2017 approximate market interest rates as at 31 December 2018. Hence their carrying value approximates their fair value.

Forward foreign exchange contracts are derivatives valued using a valuation technique with market observable inputs. The applied valuation technique for such derivatives includes forward pricing models using present value calculations.

Investment securities

As at 31 December 2018 investment securities represent fixed rated financial assets carried at amortized cost. The fair value for investment securities is derived by discounting the future cash flows using current market rates for similar financial assets.

(Amounts in tables are in thousands of Georgian lari)

21. Maturity analysis of assets and liabilities

The table below shows an analysis of assets and liabilities according to when they are expected to be recovered or settled. See Note 19 “Risk management” for the Bank’s contractual undiscounted repayment obligations.

	2018			2017		
	Within one year	**More than one year**	**Total**	**Within one year**	**More than one year**	**Total**
Cash and cash equivalents	46,503	–	**46,503**	43,908	–	**43,908**
Amounts due from credit institutions	63,105	–	**63,105**	51,445	–	**51,445**
Loans to customers	82,321	106,513	**188,834**	83,719	27,960	**111,679**
Investment securities	1,863	18,363	**20,226**	21,105	40,928	**62,033**
Property and equipment	–	2,136	**2,136**	–	906	**906**
Intangible assets	–	2,513	**2,513**	–	2,122	**2,122**
Deferred income tax assets	148	–	**148**	–	–	–
Other assets	2,557	1,035	**3,592**	495	216	**711**
Total	**196,497**	**130,560**	**327,057**	**200,672**	**72,132**	**272,804**
Amounts due to credit institutions	78,195	32,067	**110,262**	106,402	–	**106,402**
Amounts due to customers	104,228	311	**104,539**	53,682	4,499	**58,181**
Provisions for guarantees and letters of credit	6	–	**6**	135	–	**135**
Other liabilities	1,929	11	**1,940**	1,279	–	**1,279**
Total	**184,358**	**32,389**	**216,747**	**161,498**	**4,499**	**165,997**
Net	**12,139**	**98,171**	**110,310**	**39,174**	**67,633**	**106,807**

22. Related party disclosures

In accordance with IAS 24 *Related Party Disclosures*, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

(Amounts in tables are in thousands of Georgian lari)

22. Related party disclosures (continued)

The outstanding balances of related party transactions are as follows:

	2018			2017		
	The Parent	Key management personnel	Entities under common control	The Parent	Key management personnel	Entities under common control
Cash and cash equivalents	1,307	–	25	2,054	–	5,018
Loans to customers	–	82	–	–	166	–
Amounts due to credit institutions	(8,085)	–	(36,220)	(53,589)	–	(24,530)
Amounts due to customers	–	(6,807)	(24,780)	–	(6,579)	(28,140)
Other liabilities	(2)	–	–	(12)	–	–

The income and expense arising from related party transactions are as follows:

	2018			2017		
	The Parent	Key management personnel	Entities under common control	The Parent	Key management personnel	Entities under common control
Fee and commission income	–	–	1	–	–	1
Fee and commission expense	93	–	–	171	–	–
Interest income on loans to customers	–	17	–	–	16	–
Interest income on amounts due from credit institutions	(2)	–	48	(2)	–	360
Interest expense on amounts due to credit institutions	986	–	516	1,643	–	362
Interest expense on amounts due to customers	–	165	357	–	175	449
Professional fees	69	–	–	79	–	–

Compensation of key management personnel was comprised of the following:

	2018	2017
Salaries and other short-term benefits	1,753	1,548

Key management personnel as at 31 December 2018 and 2017 comprised of 5 members of the Supervisory Board and 3 members of the Board of Directors of the Bank.

(Amounts in tables are in thousands of Georgian lari)

23. Capital adequacy

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the ratios established by the NBG in supervising the Bank.

The primary objectives of the Bank's capital management are (i) to ensure that the Bank complies with externally imposed capital requirements set by the NBG and (ii) to safeguard the Bank's ability to continue as a going concern. Compliance with capital adequacy ratios set by the NBG is monitored monthly with reports outlining their calculation reviewed and signed by the Bank's Chief Accountant or Chief Financial Officer and subsequently submitted to the NBG

During year ended 31 December 2018 the Bank had complied in full with all its externally imposed capital requirements.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities.

NBG capital adequacy ratio

In December 2017 the NBG has introduced amendments to the "Regulation on Capital Adequacy Requirements for Commercial Banks". Under the updated capital framework, capital requirements are divided into Pillar 1 Requirements for Common Equity Tier 1, Tier 1 and Regulatory Capital and additional buffers under Pillar 1 and Pillar 2.

Pillar 1

- the capital conservation buffer (which was incorporated in minimum capital requirements) is separated and set at 2.5%;
- a countercyclical capital buffer is currently set at 0%;
- a systemic risk buffer will be introduced for systematically important banks over the 4 years period.

Pillar 2

- a currency induced credit risk (CICR) buffer replaced conservative weighting for un-hedged FX loans denominated in foreign currencies;
- concentration buffer for sectoral and single borrower exposure will be introduced;
- a net stress buffer will be introduced based on stress testing results provided by the Bank;
- a General Risk-assessment Programme (GRAPE) buffer defined by the regulator, based on the Bank's specific risks.

(Amounts in tables are in thousands of Georgian lari)

23. Capital Adequacy (continued)

NBG capital adequacy ratio (continued)

The NBG requires the Bank to maintain a minimum total capital adequacy ratio of 24.8% and Tier 1 / Core Tier 1 Capital ratio of 9.4% of risk-weighted assets, computed based on Basel III requirements. As at 31 December 2018 the Bank's capital adequacy ratio on this basis was as follows:

	Notes	31 December 2018	Adjustments	31 December 2018 Per the NBG
Share capital	13	103,000	–	103,000
Retained earnings		4,053	(1,840)	2,213
Less: intangible assets, net	8	(2,513)	–	(2,513)
Current period income		3,189	(615)	2,574
Core tier 1 capital		**107,729**	**(2,455)**	**105,274**
Tier 1 capital		**107,729**	**(2,455)**	**105,274**
Supplementary capital		3,020	1,020	4,040
Total regulatory capital		**110,749**	**(1,435)**	**109,314**
Risk weighted assets				**364,770**
Capital adequacy ratio				29.97%
Core Tier 1 capital / Tier 1 capital adequacy ratio				28.86%

	Notes	31 December 2017	Adjustments	31 December 2017 Per the NBG
Share capital	13	103,000	–	103,000
Prior years accumulated deficit		354	(2,149)	(1,795)
Less: intangible assets, net	8	(2,122)	–	(2,122)
Other adjustments		–	(3,888)	(3,888)
Current year income		3,453	554	4,007
Core tier 1 capital		**104,685**	**(5,483)**	**99,202**
Tier 1 capital		**104,685**	**(5,483)**	**99,202**
Supplementary capital		3,479	(523)	2,956
Total regulatory capital		**108,164**	**(6,006)**	**102,158**
Risk weighted assets				**283,322**
Capital adequacy ratio				36.06%
Core Tier 1 capital / Tier 1 capital adequacy ratio				35.01%